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SERIOUS AND LONGSTANDING DEFICIENCIES PLAGUE THE STATE DEPARTMENT'S OVERSEAS CONSTRUCTION OPERATIONS

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FORTY-THIRD REPORT

BY THE

COMMITTEE ON GOVERNMENT OPERATIONS

AUGUST 5, 1986.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

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LETTER OF TRANSMITTAL

HOUSE OF REPRESENTATIVES,
Washington, DC, August 5, 1986.

Hon. THOMAS P. O'NEILL, Jr.,
Speaker of the House of Representatives,
Washington, DC.

DEAR MR. SPEAKER: By direction of the Committee on Government Operations, I submit herewith the committee's forty-third report to the 99th Congress. The committee's report is based on a study made by its Legislation and National Security Subcommittee.

JACK BROOKS, *Chairman.*

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Mr. BROOKS, from the Committee on Government Operations, submitted the following

FORTY-THIRD REPORT

BASED ON A STUDY BY THE LEGISLATION AND NATIONAL SECURITY SUBCOMMITTEE

On August 5, 1986, the Committee on Government Operations approved and adopted a report entitled "Serious and Longstanding Deficiencies Plague the State Department's Overseas Construction Operations." The chairman was directed to transmit a copy to the Speaker of the House.

I. SUMMARY

The Department of State's Office of Foreign Buildings (FBO) is responsible for the construction of U.S. diplomatic and consular facilities overseas. FBO's present construction program—42 major projects at an estimated total cost of $1.2 billion—represents a significant investment of the taxpayers' money. These construction activities will be tremendously expanded, however, if the Department's current security construction proposal receives congressional approval. The proposed multiyear program involves 253 projects, including at least 67 new embassies and consulates, and will cost a minimum of $2.9 billion. Unfortunately, FBO's performance over the years raises serious questions about its ability to implement this ambitious program successfully.

The committee's recent review documents that serious and longstanding systemic deficiencies in FBO's operations over the years have resulted in substandard design, poor contracting procedures,

shoddy workmanship, inadequate management, lengthy delays, and major cost overruns on many construction projects. Failure to correct these problems would jeopardize efforts to provide increased security for U.S. diplomatic personnel overseas and permit continued waste of valuable tax dollars.

The State Department has initiated efforts to improve the management of FBO's construction operations. While these initiatives appear promising, additional corrective actions are needed to achieve an efficient, effective, and economical overseas construction program. In addition, these efforts will succeed only with the help of sustained personal commitment by the State Department's top management, thorough audit coverage by the Department's Office of Inspector General, and vigorous oversight by the Congress.

II. Hearings

On May 20, 1986 the Legislation and National Security Subcommittee held a hearing to review deficiencies in the management of the Department of State's overseas construction operations.[1] Testimony was presented by Joan M. McCabe, Associate Director, National Security and International Affairs Division, U.S. General Accounting Office; H. Byron Hollingsworth, Deputy Program Inspector General, Department of State; and Donald J. Bouchard, Assistant Secretary for Administration, Department of State.

III. Introduction

The Foreign Service Buildings Act of 1926 authorizes the Secretary of State to acquire, construct, maintain, operate, and sell land and buildings overseas for diplomatic and consular operations. The Secretary has delegated this authority to the Director of FBO, who serves as a Deputy Assistant Secretary under the Assistant Secretary for Administration.

FBO is divided into two functional divisions: (1) Capital Programs, and (2) Operations and Administration. The director of each division reports to the Deputy Assistant Secretary. A total of 161 staff positions are currently authorized—87 in the Capital Programs Division, 71 in the Operations and Administration Division, and 3 in the Office of the Deputy Assistant Secretary. Of the 161 authorized positions, however, 39 are currently vacant.[2]

Over the past 5 years FBO's total appropriation and the capital program portion of the total have been as follows:[3]

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[1] Hearing on "Deficiencies in the State Department's Overseas Construction Projects," before the Legislation and National Security Subcommittee of the Committee on Government Operations, May 20, 1986, 99th Congress, 2nd Session (hereinafter cited as "Hearing.") Since the hearing record will be published after the issuance of this report, references are to the stenographic transcript.

[2] Hearings.

[3] Hearing.

[In millions of dollars]

	Total appropriation	Capital program portion
Fiscal year:		
1982	$203.6	$46.0
1983	215.3	93.3
1984	207.1	62.4
1985	406.6	245.5
1986	337.0	134.5

FBO's current capital program includes 42 major construction projects in 38 countries. The projects are in various stages of completion, ranging from site acquisition to actual construction, with the last of them expected to be finished by May 1991. The estimated total cost of these projects is $1.2 billion. However, current proposals for enhancing the security of U.S. diplomatic personnel and facilities overseas would require a tremendous expansion of FBO's construction activities. The security construction proposal resulting from the recommendations of the Secretary of State's Advisory Panel on Overseas Security calls for a total of 253 projects, including the building of 67 new embassies and consulates. The Dept. has proposed funding these projects during fiscal years 1985–1990, with an actual completion date of April 1992. The projects will cost a minimum of $2.9 billion.[4]

The construction program is included in the State Department's proposed five-year, $4.4 billion diplomatic security package. On March 18, 1986 the House of Representatives approved legislation, H.R. 4151, authorizing the full $4.4 billion. The Senate approved a scaled-down security package on June 25, 1986. The Senate version authorizes $1.1 billion—including $857.8 million for construction and renovation—for fiscal years 1986 and 1987. At the time of the Government Operations Committee's consideration of this report, efforts were underway to resolve the differences between the House and Senate bills.

The State Department has acknowledged the massive scale of the proposed construction program. Assistant Secretary of State for Administration Donald J. Bouchard testified in the subcommittee's hearing that, "The program is of a scope never before undertaken by the Department of State. In a single year we will engage in as many building projects overseas as we once did in a 10-year period."[5] Unfortunately, FBO's performance over the years raises serious questions about its ability to implement this ambitious program successfully.

Between the early 1960's and 1985 the General Accounting Office (GAO) issued several reports documenting serious deficiencies in

[4] Hearing. According to the State Department, the 253 projects include "67 new Embassies and consulates, 29 relocations and/or rehabilitations of Embassies and consulates, 55 relocations and/or rehabilitations of AID (Agency for International Development) office buildings, 72 relocations and/or renovations of USIS (United States Information Service) facilities, and 30 security upgrades to VOA (Voice of America) stations." While the State Department estimates the total cost of the constrution program at $2.93 billion, projected proceeds of $280 million from the sale of current State Department properties is expected to reduce the amount of appropriated funds required to $2.65 billion.

[5] Hearing.

FBO's management of both its general operations and its construction projects. Several reports issued between 1981 and mid-1985 by the State Department's Office of Program Inspector General (formerly the Office of Inspector General) also identified serious problems in FBO's operations.

On June 18, 1985 Chairman Jack Brooks requested that GAO review FBO's management of two construction projects—an ambassador's residence and a chancery—in Cairo, Egypt. The request was prompted by reports of serious problems on the Cairo projects as well as by concerns over FBO's ability to implement the construction program then being recommended by the Advisory Panel on Overseas Security.

GAO presented its findings and recommendations at the subcommittee's hearing. In addition, the State Department's Office of Program Inspector General discussed the findings and recommendations of its reports mentioned above, as well as those of an August 1985 audit report on several FBO construction projects.

IV. Discussion

A. FBO's Cairo Projects.—A "Comedy of Errors"

Testimony on FBO's Cairo projects in the subcommittee's hearing documented what Congressman Frank Horton, the committee's ranking minority member, called "just one comedy of errors after the other." [6]

Construction of the ambassador's residence in the Giza section of Cairo was to have been completed in July 1981 at a cost of about $2 million. However, due to substandard design, poor contracting procedures, shoddy workmanship, and inadequate project management the building was still incomplete by February 1984, despite the expenditure of $3.6 million. An additional $930,000 would have been needed to make the residence habitable. Instead, FBO abandoned the project and decided to sell the land and unfinished residence. FBO paid for most of the cost overrun by reprogramming nearly $1 million from miscellaneous accounts and other construction projects without providing the required notification to Congress.

The chancery was to have been completed by January 1986 at a cost of $27.6 million. By March 1986, however, it was only one-third complete despite the expenditure of $16 million. In January 1985, FBO terminated its contract with the original contractor for nonperformance. Over a year later, in March 1986, a new contractor was selected to complete the project. The estimated cost of the chancery is now $45 million.

Finally, for several years the U.S. Government has owned three ambassador's residences in Cairo—only one of which has ever been occupied. The three include the unfinished Giza residence; the home the ambassador is actually living in—originally intended for the second ranking U.S. diplomat in Egypt; and a third residence in the El Maadi section of Cairo which was purchased in 1975 and ready for occupancy in 1978. However, despite the fact that nearly $3 million was spent on the El Maadi residence, the ambassador at

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[6] Hearing.

the time refused to live in it. His refusal was based, in part, on his determination that the residence was too isolated from the residences of other foreign ambassadors in Cairo. The building has remained vacant since its renovation and FBO is currently in the process of selling it.

These projects are discussed in greater detail below.

The Ambassador's Residence in Giza

In October 1975, FBO awarded a fixed-price contract of $180,300 to a Washington, D.C., architectural and engineering (A&E) firm for the design of the ambassador's residence in the Giza section of Cairo. Eleven amendments for various services, including site inspections during construction, brought the total cost of the contract to $373,239.[7] Unfortunately, FBO failed to assure that it got its money's worth.

The most serious deficiency in the residence design was that it failed to specify the use of U.S. building standards, as required by FBO's regulations. Lax Egyptian standards were followed instead. The failure to use U.S. standards contributed significantly to the construction problems experienced on the project. For example, the design did not require the use of "pipe chases," channels through which plumbing pipes or wiring is passed. As a result, plumbing pipes were embedded directly in the masonry. This made it extremely difficult and expensive to correct subsequent leaks in the pipes.

The State Department is unable to provide a reasonable explanation for its failure to assure adherence to U.S. standards. In testimony before the subcommittee, Assistant Secretary Bouchard simply stated that, "There is no evidence in the file that would indicate why standards that are normally unacceptable to FBO were allowed in this particular project." [8]

Other major problems with the design contract included the A&E firm's failure to provide an adequate estimate of construction materials and labor costs, and its failure to develop a comprehensive feasibility study for the project, as required by the contract.

The construction contract for the residence was awarded in June 1979, with completion scheduled for July 1981. The procurement procedures used to select the construction contractor, however, were seriously flawed. The most significant deficiency was FBO's failure to evaluate thoroughly the technical capabilities and financial condition of the two firms competing for the contract. Both were certified simply on the basis of having previously performed renovation and remedial work on the U.S. Embassy and participated as subcontractors in the construction of an apartment complex for embassy staff. However, according to the State Department's Program Inspector General:

> A cursory examination of the two bidders would have revealed that they did not actually own fully outfitted construction companies, but were merely construction brokers who subcontracted virtually all of the trades work. In the

[7] U.S. Department of State, Office of the Inspector General, "Report of the Special Inquiry Into the Construction of the Embassy Residence at Giza, Cairo, Egypt, October 1984, p. 9.

[8] Hearing.

> case of El Abd (the winning bidder), an examination of the work performed by his firm at the U.S. embassy would have revealed both substandard workmanship and a lack of basic electrical safety features of construction.[9]

While contending that the contractor's financial and technical capabilities were, in fact, reviewed by FBO prior to the award of the contract, the State Department told the subcommittee that:

> . . . On the basis of information available in the files, the contractor would not be awarded the contract under current technical and financial qualification and evaluation standards.[10]

Defective materials and shoddy workmanship plagued the project. For example, the contractor used substandard plumbing pipe and electrical conduit; the plumbing subsequently leaked and the conduit quickly rusted and deteriorated. With respect to the quality of construction, the Program Inspector General concluded, "There are many examples of workmanship that [are] so poor that it is hard to believe that anyone other than totally unskilled labor was involved." [11] Among the most blatant cases of shoddy work was a bathtub drain pipe that emptied directly onto a bedroom balcony.

FBO's management of the residence's construction—both on the part of its onsite project manager and on the part of FBO headquarters—was seriously deficient. According to GAO, the project manager failed to ". . . monitor construction closely, reject unsatisfactory materials and workmanship, and report problems fully to headquarters," and headquarters failed to "properly support" the manager with "technical advice and staff." [12]

A particularly flagrant example of poor management involves the response of the project manager and headquarters to onsite inspection reports filed by a consultant working for the design contractor. In January 1980, the consultant reported to both the project manager and headquarters that substandard pipes and conduits were being used. The consultant continued to report similar deficiencies as work progressed. Nevertheless, according to GAO:

> . . . the site manager's monthly reports to FBO headquarters did not indicate whether the identified defects were corrected. In fact, his reports did not always refer to the defects and appeared to indicate that adequate progress was being made. *For almost 2 years, FBO headquarters staff did not question the project manager concerning defects identified in the consultant's inspection reports.* (Italics added.) [13]

Commenting on the failure to address the problems identified by the consultant, the Program Inspector General stated, ". . . the lack of followup action on the part of the project manager and his

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[9] Ibid, note 7, p. 18.
[10] Hearing.
[11] Ibid, note 7, p. 36.
[12] Hearing.
[13] U.S. General Accounting Office report, "Problems in Constructing Embassy Facilities in Cairo, Egypt," NSIAD–86–101, April 18, 1986 (hereinafter cited as GAO report), p. 5.

superiors characterized the mismanagement of the project throughout its life." [14]

The total inadequacy of FBO's management of the project is further illustrated by the lack of timely site visits by headquarters staff with technical expertise. According to the Program Inspector General,

> Although A/FBO Director (William) Slayton and other nontechnical officers visited the site several times during critical phases of construction, *no A/FBO officer possessing technical skills visited the post until May 1981, almost two years after the project started.* (Italics added.) [15]

In June 1982—3 full years after the award of the contract and nearly a year after the originally scheduled completion date—work under the original construction contract was suspended because of "a sustained period of poor productivity and the contractor's lack of responsiveness to FBO directives." [16] Over the next year and a half, extensive remedial work was done by other contractors in an effort to correct serious deficiencies in the residence.

By February 1984, however, all available funds were exhausted. Despite the expenditure of $3.6 million—$2.63 million for the original contract and change orders, and $925,266 for remedial work—the residence was still uninhabitable. An estimated $930,000 would have been needed to complete the building. Instead, FBO abandoned the project and decided to sell the land and unfinished house.

The impact of FBO's mismanagement of this project was compounded by FBO's failure to protect the U.S. Government's interests from substandard performance by the original construction contractor. While FBO obtained a performance bond equal to 10 percent of the original contract price, the bond was allowed to expire; no funds were recovered. The State Department's explanation for the failure to file a claim against the bond simply underscores the inadequacy of FBO's internal management controls. According to the Department:

> The performance bond from the prime contractor was allowed to expire because *there was no evidence that the work was not substantially complete,* although there was no Certificate of Substantial Completion. Each inquiry about the substantial completion was answered by assurances that the work would be complete within a short period of time. When engineers from FBO Washington were able to visit Cairo and ascertain the extent of the problem, introduction of additional contractors to the project site had compromised the Government's position to such a degree that a termination for default and/or action against the surety could not be sustained. . . .[17]

FBO paid for much of the cost overrun on the ambassador's residence by reprogramming nearly $1 million without providing the

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[14] Ibid, note 7, p. 4.
[15] Ibid, p. 38.
[16] GAO report, p. 14.
[17] Hearing.

required notification to Congress. The funds were transferred, primarily in fiscal year 1980, from miscellaneous accounts and other construction projects in Cairo. The House and Senate Appropriations Committees' reports for that year called for the State Department to provide the two committees with prior notification of any reprogrammings exceeding $250,000 or 10 percent of a program or activity's funding, whichever was less.

There is no clear explanation as to why FBO failed to notify the Appropriations Committees of the reprogrammings. Notification letters were drafted but never sent. According to the State Department:

> The reprogramming may have been the result of unintentional oversight. There was no mechanism which could guarantee enforcement of this (notification) requirement. While it is clear that FBO did not notify Congress of its intent to reprogram, records do not indicate why such action was taken. . . .[18]

During its review of the ambassador's residence project, an audit team from the Department's Office of Program Inspector General interviewed William Slayton, the Director of FBO at the time of the reprogrammings. Mr. Slayton acknowledged that notification was required and concluded, "We must have goofed." [19]

In summary, despite the expenditure of $3.6 million over a 9-year period, FBO failed to produce a residence suitable for the U.S. ambassador to Egypt. In commenting on the project during the subcommittee's hearing, Assistant Secretary Bouchard observed that, ". . . It was a total disaster from inception to where we are today . . ." [20] The committee shares the Assistant Secretary's view.

The Chancery

In September 1979, FBO awarded a contract to an architectural and engineering firm for the design of a 20-story chancery in Cairo. Nine months later, however, the contract was cancelled because of a controversy over the height of the proposed building. After a study of alternative designs, a second design contract was awarded in September 1980—this time for a 16-story building. According to GAO, the lower height was due to the fact that "some post officials (in Cairo) believed a 20-floor building would be too ostentatious and would symbolize the growing role of the United States in Egypt." [21] The design was subsequently changed again. This change, however, increased the height of the building. According to the State Department, the building will now have 16 stories "and a small roof structure" when completed.[22]

In November 1982, FBO awarded a $27.6 million construction contract for the chancery to an Egyptian firm. The scheduled completion date was January 1986. According to GAO, however, FBO's choice of contractors was "questionable" because (1) FBO failed to

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[18] Hearings.
[19] Ibid, note 7, p. 43.
[20] Hearing.
[21] GAO report, p. 4.
[22] Hearing.

perform an in-depth analysis of the firm's financial condition, (2) the firm had limited experience, and (3) key technical and management personnel left the firm prior to the award of the contract.[23]

Lax internal procedures contributed to FBO's failure to select a competent contractor. According to GAO:

> While FBO collects some financial data on potential contractors, *it has no written procedures for interpreting or analyzing the data or for evaluating financial capabilities relative to the work under consideration* . . . (Italic added.)[24]

As with the Giza residence, FBO's poor choice of contractors doomed the chancery project. Within a year after the award of the construction contract, subcontractors began to complain that the general contractor was falling behind in its payments to them. Between November 1983 and January 1985, FBO took numerous steps intended to enable the general contractor to work out financial arrangements with its subcontractors. These efforts proved unsuccessful, however, and work on the chancery eventually stopped. On January 13, 1985, FBO terminated the contract for nonperformance. Despite the expenditure of about $16 million, the chancery was only one-third complete. Interim work was performed by one of the original subcontractors while FBO solicited bids from other firms to complete the project.

A new contract was awarded in February 1986. The estimated total cost for the project—including redesign costs and interim work—now stands at $45 million, as opposed to the original estimate of $27.6 million. The increased costs are in part due to the expense of meeting new State Department security requirements. According to the Department, the chancery is now scheduled for completion in July 1988—2½ years later than originally expected.

The Ambassador's Residence in El Maadi

In November 1975, FBO purchased a home in the El Maadi section of Cairo for use as the U.S. ambassador's residence. The purchase price was $1.8 million, and FBO subsequently spent an additional $1.1 million for extensive renovation work.

The residence was ready for occupancy in 1978. The ambassador, however, refused to move into the house. His refusal was based on security considerations, dissatisfaction with the length of the commute to the embassy, and his belief that the home was too isolated from the residences of other ambassadors in Cairo. In addition, the embassy found that Egyptian government officials would not travel out to the El Maadi section for meetings or representational functions. The ambassador decided to remain in a house in the Zamalek section of Cairo that had originally been used as the Deputy Chief of Mission's (DCM) home, but which had served as the ambassador's residence since 1973. All subsequent ambassadors to Egypt have lived in the Zamalek residence as well.

As a result of the determination that the house in El Maadi "would not be satisfactory for an ambassador's residence," FBO de-

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[23] GAO report, p. 6.
[24] Ibid.

cided to sell the property. In June 1982, FBO signed a preliminary agreement to sell the residence for $2,467,295—about $466,000 less than its purchase and renovation costs for the property. Four years later, however, the transaction is still not complete. According to the State Department, while the Egyptian government has approved the sale, "The transfer of title remains in process."[25]

The committee finds the State Department's lack of proper planning on the El Maadi residence totally inexcusable. Specifically, the committee is unable to understand the Department's apparent failure to determine the acceptability of the El Maadi residence *before* spending nearly $3 million on it. Responding to a question from Chairman Brooks in the subcommittee's hearing, Assistant Secretary Bouchard concluded that the Department's mismanagement of this matter, ". . . is part of the Cairo fiasco. We have no explanation."[26]

The committee also notes that the Department's argument concerning the suitability of the El Maadi residence is undercut by GAO's testimony. According to GAO, apartments for U.S. embassy staff are located in El Maadi and FBO is currently building additional staff housing there. In addition, ambassadors from other countries reside in El Maadi.

The Sale of the Ambassador's Residence in Giza

As noted earlier, FBO's unsuccessful efforts on the ambassador's residence in the Giza section of Cairo led to a decision to sell the property. In January 1986, FBO reached an agreement to sell the land and unfinished house to an Egyptian investment group for about $16 million. Taxes of approximately $3.2 million on the sale will leave the U.S. Government with net proceeds of $12.8 million. At the time of the subcommittee's hearing, the purchaser had paid for the property but the title had not yet changed hands. On July 10, 1986, however, U.S. embassy officials in Cairo signed the final deed of sale.[27]

The unfinished residence is located on a prime parcel of land overlooking the Nile River. The property was purchased by the U.S. Government in 1968 for only $161,000. While it may not have been advisable to attempt the work that would have been needed to complete the residence, the committee believes the site could have served as the choice location for an ambassador's residence in the future.

On the other hand, the building currently being used as the ambassador's residence is a small house in the Zamelek section of Cairo originally used by the DCM. Former U.S. Ambassador to Egypt Hermann F. Eilts, who lived in the house for several years, has described the residence as "Too small for the ambassadorial function and . . . also a distinct security risk."[28] Nevertheless, during the subcommittee's hearing the State Department defended this house as meeting the U.S. Government's needs for an ambassador's residence in Cairo.

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[25] Hearing.
[26] Hearing.
[27] Hearing; cable to FBO from U.S. Embassy, Cairo, Egypt.
[28] Hearing; letter to the Editor, Washington Post, from Hermann Fredrick Eilts, former U.S. Ambassador to Egypt, June 17, 1986.

The Department's claims, however, are called into question by information provided to the subcommittee by GAO after the hearing. According to GAO, the Department has determined that the residence is too small and must be expanded. The Department later acknowledged the expansion project, which is expected to cost $64,500. (Despite the fact that the subcommittee specifically asked the Department to describe its "current long-range plans for providing a residence for the U.S. ambassador to Egypt," the Department failed to inform the subcommittee of the expansion project until asked to confirm the information provided by GAO.) Claims as to the adequacy of the Zamelek residence ar further undercut by the fact that the house had obviously been deemed inadequate in the past since a decision was made to build a new residence at the Giza site.

Finally, should the Department decide to build or purchase a new ambassador's residence in Cairo in the future, the tremendous appreciation of the Giza parcel over the past 18 years indicates that it would be extremely expensive to acquire another desirable location.

After the subcommittee's hearing, GAO investigated the status of the Giza property's sale. State Department officials in Washington, D.C. advised GAO staff to contact the U.S. Embassy in Cairo for information relating to the sale. On June 4, 1986, the Administrative Officer at the U.S. Embassy in Cairo, after having consulted with Egyptian attorneys representing the Embassy in the transaction, told GAO staff that there appeared to be no legal obstacles to cancelling the sale; the Department would simply have to return the $16 million to the purchaser.[29]

On June 11, 1986 Chairman Brooks wrote Secretary of State George Shultz concerning the sale of the Giza property. Citing the desirability of the Giza parcel for a future ambassador's residence and the inadequacies of the Zamelek residence, the Chairman urged the Secretary to cancel the sale.

On July 7, 1986 the State Department replied to the Chairman's letter. The Department again argued that the current ambassador's residence is adequate. Furthermore, it contended—in direct contradiction to what GAO investigators had been told—that "under Egyptian law we are committed to the sale."[30]

The committee believes that the State Department has failed to make a persuasive case that the decision to sell the Giza property was in the U.S. Government's best interests. In addition, it is concerned about the discrepancies between what the Department told GAO concerning the legal status of the sale and what it told Chairman Brooks on this matter. The committee, therefore, requests that the State Department provide detailed documentation to support its claim that it was required by Egyptian law to complete the sale of the Giza property.

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[29] Hearing; letter to Chairman Brooks from Robert L. Higgins, Assistant General Counsel, U.S. General Accounting Office, July 29, 1986.

[30] Hearing.

B. THE "CAIRO FIASCO" WAS NOT AN ISOLATED CASE

While testimony in the subcommittee's hearing indicated that FBO has produced some successful construction efforts, its mismanagement of the Cairo projects has been an all-too-common story. When asked by Chairman Brooks to compare GAO's findings on Cairo with the results of previous GAO reviews of FBO operations, Joan M. McCabe, Associate Director of GAO's National Security and International Affairs Division, replied that:

> . . . the problems evidenced in Cairo were fairly common and were not new. In our past work, we found problems such as cost overruns, delays in construction due to design changes, inadequate technical assistance, contracting with unqualified contractors, lack of long-range plans, many of the same problems that affected the projects in Cairo.[31]

Similarly, audits conducted by the State Department's Office of the Program Inspector General over the past several years identify several unsuccessful projects besides those in Cairo and document serious systemic deficiencies in FBO's operations. H. Byron Hollingsworth, the State Department's Deputy Program Inspector General, discussed some of these audits in the subcommittee's hearing. They are summarized below.

FBO's Procurement Procedures

In January 1981, the Office of Program Inspector General issued a report on FBO's procurement policies and procedures. According to Mr. Hollingsworth, the report documented

> . . . control weaknesses in FBO contracts in general, and in architectural and engineering (A&E) contracts in particular. Documentation for A&E contracts was totally inadequate to support decisions for selecting A&E firms, the selection process was weak, and FBO was not following its own policy of limiting A&E firms to no more than one major project.[32]

FBO's response to the report's recommendations was less than fully satisfactory. Mr. Hollingsworth noted that while FBO implemented some of the recommendations, it rejected others. As a result, subsequent Program Inspector General audits found that many of these same deficiencies continued to plague FBO's procurement operations. (Weaknesses in FBO's procurement procedures for A&E contracts are discussed in greater detail later in this report.)

The Khartoum Office Building/Chancery Project

In November 1981, the Program Inspector General issued a report on the renovation of a new office building/chancery in Khartoum, Sudan. The project was plagued by major cost overruns and delays.

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[31] Hearing.
[32] Hearing.

In September 1979, the U.S. Embassy in Khartoum signed a 5-year lease at $264,000 per year for an eight-story newly constructed apartment building. The building was to be renovated to serve as an office building/chancery. The renovation project was to be completed by June 1, 1980 at a cost of $500,000. Instead, the building was not ready for full occupancy until late September 1981. While precise cost data are unavailable, the Program Inspector General estimates that the project may have cost as much as $2.5 million—five times the original estimate. An additional $528,000 was spent for rent over the 2 years the building remained vacant.

Various organizational components of the State Department—FBO, the Bureau of African Affairs, the Office of Communication, and the Office of Security—were involved in the project. According to the Program Inspector General's report, however, "Responsibility for planning, coordinating and monitoring the Khartoum project was never clearly defined, and as a consequence, became a 'hot potato' of bureaucratic juggling" between FBO and the Bureau of African Affairs.[33] Mr. Hollingsworth told the subcommittee that this lack of planning and coordination:

> . . . resulted in an incomplete design, inadequate specifications, structural problems, and repeated changes in facilities requirements and space layouts . . . Overall, this project was poorly managed and controlled, and was excessively costly.[34]

FBO's Management Information Systems

A September 1982 audit report by the Program Inspector General assessed the quality of FBO's management information systems. The review covered a wide range of systems—budget, financial management, real property management, design and construction management, etc. In the subcommittee's hearing, Mr. Hollingsworth testified that the audit revealed:

> . . . significant shortcomings in data collection for control of projects, particularly data regarding costs, both estimated and incurred. We concluded that FBO could not manage its worldwide properties and construction programs in an effective and efficient manner until it had complete and accurate information on the properties and programs.[35]

The report concluded that while FBO had made progress in improving its performance, it

> . . . *still suffers from a credibility gap* that can only be reduced through determined efforts by management to provide itself with the tools it needs to make informed judgments and to follow through on its decisions. These, in turn, require the setting in place of all the elements necessary for a real estate management system. Then, and only

[33] U.S. Department of State, Office of the Inspector General, "Audit of Renovation of New Office Building/Chancery, Khartoum, Sudan, November 1981, p. 6.
[34] Hearing.
[35] Hearing.

then, will management of FBO function at a level equal to its substantial responsibilities. (Emphasis added.) [36]

The Senior Officers' Residences in New Delhi

A 1984 Program Inspector General review found serious deficiencies in FBO's effort to build four residences for senior Foreign Service officers in New Delhi, India. The project's problems were similar to those of the unfinished ambassador's residence in Cairo: inferior construction materials, shoddy workmanship, poor on-site management, inadequate support from FBO headquarters, major cost overruns, and lengthy delays. And, as is the case of the ambassador's residence, the project's contractor ultimately defaulted.

Begun in October 1979, the project called for the construction of two buildings, with each one containing two residences. The four residences were to be completed in 1 year at a total cost of $1 million. After 4 years, however, the residences were still unfinished despite the expenditure of $1.8 million. The contract was terminated on the basis on contractor default.

The project's cost overruns were due to 35 change orders, most of which were overpriced. For example, a change order designed to provide earthquake protection for the residences cost $328,000. However, according to an analysis by the Program Inspector General's audit team, the change order should have been priced at only $60,000.

The contractor used materials inferior to those specified in the contract, but charged FBO full price. In addition, workmanship on the project was shoddy. A particularly egregious example of poor construction was discovered when a plumbing leak resulted in one of the unit's floors sinking. Upon investigation, it was found that the contractor had not properly compacted the soil beneath the unit and had not installed a concrete slab beneath the floor, as required by the contract. There were also serious problems with the plumbing, air conditioning, mechanical, and finishing work. Finally, both onsite management and oversight from FBO headquarters were inadequate.

Neither building was finished at the time of the contract's termination. Upon termination, the contractor turned one building over to FBO. It was occupied in January 1983, but only after extensive remedial work by embassy staff. The contractor, however, refused to relinquish possession of the other building due to unresolved contract disputes. Despite the fact that the building is on land owned by the U.S. Government, the contractor posted armed guards to deny access to U.S. personnel and representatives.

The contractor filed suit against FBO in the U.S. Armed Forced Board of Contract Appeals, as provided for in the contract. According to the State Department, on December 18, 1985 the Board found in favor of FBO on all points and assessed damages of $326,300. Nevertheless, FBO is considering on out-of-court settlement "in light of the probable difficulties in enforcing a U.S. legal decision in India." [37]

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[36] U.S. Department of State, Office of the Inspector General, "Management Audit of Management Information Systems, Office of Foreign Buildings, Bureau of Administration," September 1982, p. 2.

[37] Hearing.

"A Myriad of Systemic Problems"

In 1984, the Program Inspector General initiated a functional audit of FBO's construction program. The audit was undertaken to determine whether deficiencies found in the New Delhi and Giza projects were "isolated instances of inadequate construction management" or the result of inherent weaknesses in FBO's operations. The audit report was issued in August 1985. While noting that FBO had produced some successful projects, the report's overall conclusion was that "FBO construction projects continue to experience a myriad of systemic problems. . . ." [38]

In the subcommittee's hearing, Deputy Program Inspector General Hollingsworth testified that the deficiencies indentified by the audit included:

> . . . insufficient staff and/or expertise to insure effective and consistent oversight of construction projects; inadequate procedural guidance and requirements for construction project managers; insufficient controls over the award and adminstration of contracts; and, unnecessary deviations from requirements of the Federal Acquisition Regulation.[39]

One of the several projects covered by the audit was a 26-unit staff apartment in Hong Kong. The Program Inspection General's conclusions have an all-too-familiar rings:

> The Hong Kong . . . (project) . . . is a classic example of an unsuccessful project which, from the start, has been characterized by design deficiencies, poor workmanship, and contractor disputes. This resulted in excessive costs due to remedial work, severe maintenance problems, and contactors' claims. The ingredients necessary for a successful project were not present—design was not totally adequate, on-site management and central office support were insufficient, and the contractor's technical competence was questionable.[40]

As a result of design deficiencies and poor workmanship, the walls of the six-building complex developed extensive leaks. While FBO spent $300,000 to correct the problem, the Program Inspector General concluded that within the next few years the buildings will need completely new exteriors to solve the leakage problem. The estimated cost of the new exteriors is about $1 million.

Begun in March 1981, the apartment complex was to be completed by September 1982, at a cost of $5.7 million. It was not actually finished, however, until November 1985—38 months behind schedule. As a result of cost overruns, the final price tag was $7.8 million. In addition, since the expected occupants of the apartments were living in leased quarters costing about $50,000 per month, the 38-month delay cost the U.S. Government another $1.9 million.

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[38] U.S. Department of State, Office of the Inspection General, "Functional Audit of New Construction by the Office of Foreign Buildings Operations," August 1985, p. 6.
[39] Hearing.
[40] Ibid, note 38, p. 13.

Another Hong Kong project covered by the Program Inspector General's audit was a 79-unit staff apartment tower. Since the 34-story tower was only in the early stages of construction at the time of the audit team's visit, detailed findings could not be developed. The report noted, however, that while the quality of the building appeared acceptable, onsite project management was inadequate. More importantly, because of serious flaws in FBO's arrangement with the construction contractor, FBO has little leverage to assure adequate performance by the firm.

The staff apartment tower was part of a so-called "entrepreneurial" project under which FBO transferred five U.S. Government properties worth approximately $20 million to a developer. In return, the developer was required to build the apartment tower, a consul general's residence, five senior officers' residences, and provide the U.S. $2 million. The agreement called for the developer to lease the apartment tower to the Government for 10 years at a total cost of $43 million, with the U.S. holding an option to buy the tower for one dollar at the end of the lease.

FBO's control of this entrepreneurial project was serious weakened by the fact that the five properties were transferred to the developer prior to construction. In an effort to protect the Government's interests, FBO required the developer to obtain a $20 million letter of credit in favor of the United States. FBO, however, failed to execute the letter of credit when disputes arose with the contractor.

The Program Inspector General concluded that because of FBO's limited leverage, "the quality of the buildings acquired through this agreement will be whatever the developer is willing to give." [41] In the subcommittee's hearing, the Department was unable to provide a solid rationale for its decision to transfer the properties prior to completion of the project. The committee is appalled by FBO's failure to safeguard the Government's interests on this project.

In addition to identifying problems in individual projects, the Program Inspector General documented across-the-board deficiencies in FBO's construction management policies and procedures. Among the problems found were:

The lack of a formal value engineering program. (Value engineering involves reviewing construction designs to identify opportunities for reducing costs while maintaining quality.);

Inadequate controls for assuring that change orders are reasonably priced;

Weak procedures for protecting the Government's interests from improper contractor claims for additional funds;

Poor controls over negotiated contracts;

Inadequate internal regulations governing the use of performance bonds;

The absence of formal criteria for including advance payment provisions in contracts; and

The lack of an accident prevention program for construction projects.

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[41] Ibid, p. 31.

The Program Inspector General also identified weaknesses in FBO's procurement procedures for architectural and engineering services. The report concluded.

> . . . contracting procedures for A&E services are not formalized, are not sufficient, and lack adequate internal controls to ensure that contracts are awarded to the most technically qualified firms at fair and reasonable prices. Specifically, improved procedures and controls are needed for selecting A&E firms, for negotiating A&E contracts, and for administering contracts and controlling the amendment process.[42]

In testimony before the subcommittee, Mr. Hollingsworth summarized the results of the Program Inspector General's audit as follows:

> I would like to emphasize that, in our opinion, the most critical of all the deficiencies noted during our audit of new construction was the lack of effective oversight of construction projects. *If poor quality buildings are constructed the Government will not get what it paid for, and will be forced to deal with costly maintenance and remedial work for many years to come.* (Emphasis added.)[43]

The committee wholeheartedly agrees with Mr. Hollingsworth's assessment.

In an effort to correct the myriad of systemic deficiencies found during this and other audits, the Program Inspector General's report recommended sweeping revisions in FBO's operations. These recommendations are included as an appendix to the committee's report.

C. THE STATE DEPARTMENT'S EFFORTS TO IMPROVE FBO'S PERFORMANCE

While acknowledging the problems that have plagued FBO construction projects, Assistant Secretary of State Bouchard told the subcommittee that these deficiencies reflected the "old way of doing business," and that "FBO today is not the same organization it was a few years ago." According to Mr. Bouchard, recent and planned changes to FBO's operations will result in "efficient and cost-effective implementation" of the Department's proposed construction program.[44]

The heart of the Department's effort to improve FBO's performance is a plan to rely heavily on the private sector for construction management expertise. While the Secretary of State's Advisory Panel on Overseas Security recommended that the Department add over 1,000 new people to FBO, the Department concluded that such a "massive expansion of FBO's staff was not the solution" for implementing the proposed construction program. Instead, the Department opted for what it describes as a "balanced plan to reorganize and support FBO."[45] The proposal calls for a 177-person in-

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[42] Ibid, p. 25.
[43] Hearings.
[44] Hearing.
[45] Hearing.

crease in FBO's staff combined with extensive contracting with private firms for program management services.

On April 10, 1986 the State Department issued a Request for Proposals (RFP) for "highly integrated management support services" to assist FBO in carrying out its overseas building program. The RFP calls for the "program management contractor" to develop many of the basic internal policies, procedures, and systems needed for the program, as well as to handle most of the day-to-day management responsibilities for 13 specific projects. The specific categories of services required are: (1) program management, (2) design and engineering management, (3) construction management, (4) operations management, (5) security management, and (6) special technical services. The contract is for 3 years at an estimated 200,000 staff hours per year. Two 1-year options to extend the contract are included. The Department expects to award the contract in late August 1986. Contracts for program management services for other groups of construction projects are expected to be awarded in the future.

The committee believes that the private sector can serve as a valuable source of management expertise for FBO's construction program. It is, however, absolutely essential for FBO to establish strong internal controls for monitoring the performance of the program management contractors. The Government's interests must be protected.

Deputy Assistant Secretary Dertadian assured the subcommittee that FBO will develop "very strict" controls over those providing program management services:

> . . . It is going to be almost micro-management in terms of FBO overseeing what the program manager does, but it is the kind of management that is needed to make sure we are getting what we are paying for and the quality of work we want.[46]

Similarly, Assistant Secretary Bouchard the told the subcommittee:

> We do not intend to hand the project to the private sector and wait for it to hand us the key . . . We intend to work hand-in-hand with the program manager, defining the scope of work and monitoring progress. FBO will make the design, construction, and budget decisions.[47]

The committee is encouraged by the Department's pledges and urges it to make the establishment of strong controls over the private sector program management contractors a top priority.

According to Mr. Bouchard, other important components of the Department's implementation plan for the proposed construction program include:

(1) "fast track and design/build" techniques intended to shorten the time needed for projects' design and construction;

(2) "risk analysis, constructability and value engineering reviews" intended to assure that projects' designs are both cost-

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[46] Hearing.
[47] Hearing.

effective and compatible with "local conditions, material availability and technical capabilities";

(3) "upgraded contractor qualification requirements" aimed at assuring that construction contracts are awarded only to firms with the necessary "financial, organizational and technical capabilities";

(4) "sufficient resources for on-site construction oversight and inspection"; and

(5) implementation of recommendations from a study on embassy security conducted by the National Academy of Sciences.[48]

Mr. Bouchard also testified that as a result of recent improvements in FBO's operations, 11 of the 13 construction or renovation projects funded under the fiscal year 1985 "security supplemental" appropriation[49] are going well. (Projects in Kuwait and Damascus have been delayed because of negotiations with the host countries.) The committee notes, however, that 3 of the 11 projects underway are behind schedule,[50] and at least 5 of the 11 have not yet reached the construction phase.[51] Further, the committee notes that the cost of the 13 projects has increased dramatically—from an original estimate of $177.5 million to a current figure of about $266 million.[52] According to GAO, the increase is primarily due to the expense of meeting new State Department security requirements.

Finally, the Department has agreed to implement all the recommendations contained the Program Inspector General's August 1985 audit report on FBO. While the committee is pleased by these pledges of corrective action, it notes that many of these changes have not yet been put in pace. For example, FBO has indicated that the private sector program manager will be responsible for implementing several of these recommendations. The committee, will, therefore, closely monitor FBO's activities to assure full implementation of the Program Inspector General's recommendations. In this connection, the committee requests that the Department provide, within 30 days, a written report on the status of its efforts to implement the Program Inspector General's recommendations.

D. UTILIZING THE EXPERTISE OF THE ARMY CORPS OF ENGINEERS

While the private sector can play an important role in the management of FBO's construction operations, there is also a valuable source of construction management expertise within the Federal Government—the Army Corps of Engineers.

The Corps of Engineers manages about $8 billion in engineering and construction work around the world each year.[53] Its activities

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[48] Hearing.

[49] The funds were provided in two separate appropriations: P.L. 98-473, October 12, 1984; and P.L. 99-88, August 15, 1985.

[50] U.S. Department of State, Report on Obligations of the FY 1985 Security Supplemental Funds" (as of March 31, 1986), Date of report, May 2, 1986.

[51] Hearing.

[52] Hearing.

[53] U.S. Army Corps of Engineers, "Fact Sheet," Subject: "Corps of Engineers Support for Others (SFO) Program," May 13, 1986.

range from civil works water projects to military air bases. In addition to its headquarters staff in Washington, D.C., the Corps maintains 14 divisions, including six overseas divisions. The staff is comprised of about 40,000 civilian and 1,000 military personnel.[54]

An important component of the Corps' activities is its "Support for Others" (SFO) program. Through this program the Corps provides planning, engineering, construction management, real estate support, and research and development support on a reimbursable basis to other Federal agencies, public entities, and foreign governments. The Corps is currently providing the full-time equivalent of over 900 persons under SFO agreements. Among the Federal departments and agencies new receiving services from the Corps are the Environmental Protection Agency, Department of Energy, Department of the Interior, Federal Emergency Management Agency, and the Voice of America.[55]

The Corps has expressed a great deal of interest in participating in the State Department's proposed security construction program. It has offered the Department a broad range of assistance including: (1) serving as overall program manager, (2) managing construction projects in countries in which it has an established "construction management presence" but the Department does not, and (3) providing support in "functional portions" of the proposed program.[56]

The State Department and the Corps have discussed possible Corps involvement in the proposed construction program, but the Department apparently does not envision a major role for the Corps. While the Department has offered to use Corps personnel—particularly construction project engineers—to help meet its increased staffing requirements, and has invited the Corps to respond to the RFP for program management services, the Department told the subcommittee that it believes there are drawbacks to using the Corps as program manager:

> . . . While we are aware of the Corps' interest in assisting on the program, there are some formidable built-in problems with the idea of effectively implementing a major construction program through the layering of two government bureaucracies which operate under different legislative authority, differing contract and procurement regulations and different management structures. . . .[57]

The State Department's lack of enthusiasm for using the Corps has resulted in the Corps deciding not to submit a proposal in response to the Department's first RFP for program management services.While the Corps views itself as "eminently qualified" [58] to perform this role, it has determined that:

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[54] U.S. Army Corps of Engineers, briefing document, "Program Support Services to the Office of Foreign Building Operations, U.S. Department of State," January 1986.

[55] Ibid, note 53.

[56] Hearing; letter to Donald J. Bouchard, Assistant Secretary of State for Administration and Security (Designate), from Secretary of the Army, John O. Marsh, Jr., September 30, 1985; and letter to Mr. Bouchard from Assistant Secretary of the Army (Civil Works), Robert K. Dawson, March 3, 1986.

[57] Hearing.

[58] Hearing; letter to Donald J. Bouchard, Assistant Secretary for Administration, Department of State, from Assistant Secretary of the Army (Civil Works), Robert K. Dawson, May 22, 1986.

> . . . State's public statements and activities over the past six months provide every indication that the services would be supplied by the private sector. This has generated such substantial private sector interest that it would be inappropriate, without clear instructions from the Administration and Congress, for the Corps to place itself in direct competition with private sector firms.[59]

Despite this decision to withdraw from the first round of competition, the Corps has told the State Department that it "remains interested in supporting you on this program and would like to be considered as a program management alternative for future phases of the effort." [60]

Notwithstanding the State Department's concerns, the committee views the Corps of Engineers as a valuable source of construction management expertise. It recommends, therefore, that the Department utilize the Corps to the fullest extent practicable in implementing its security construction program. Furthermore, while the committee understands the Corps decision not to submit a proposal in response to the Department's first RFP for program management services, it sees no reason why the Corps should not compete for future program management contracts.

E. THE NEED FOR GREATER CONTINUITY IN FBO'S MANAGEMENT

The committee is encouraged by the State Department's current and proposed efforts to improve FBO's performance. These efforts have not, however, adequately addressed a major flaw—the lack of continuity in FBO's top management. The committee believes that failure to correct this deficiency would seriously threaten the prospects of FBO successfully implementing the proposed security construction program.

Rapid turnover of top management often thwarts efforts to assure accountability for an organization's performance. In FBO's case, this problem is vividly illustrated by the history of the Cairo projects. FBO has had four different directors over the 11-year period involved. As a result, it is difficult to hold specific persons accountable for the "Cairo fiasco."

Testimony by GAO in the subcommittee's hearing identified another problem resulting from frequent changes in FBO's top management. Responding to a question from Chairman Brooks, Associate Director Joan McCabe stated:

> . . . The problem with high turnover is compounded by the fact that normally the top management in FBO does not have a construction background. Top management positions are usually filled on a rotational basis from foreign service officers. Consequently the learning curve in the construction business can be quite significant, and that is a disadvantage when you are operating such a complex program.[61]

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[59] Hearing; letter to Randall F. Davis, Associate Director, Natural Resources Division, Office of Management and Budget, from Assistant Secretary of the Army (Civil Works), Robert K. Dawson, May 22, 1986.

[60] Ibid, note 58.

[61] Hearing.

The committee notes that the current Director of FBO, Deputy Assistant Secretary Richard N. Dertadian, and the two Deputy Directors of FBO are all Foreign Service officers with little or no construction management experience prior to their current assignments. The Deputy Director for Capital Programs, who was appointed to that post in October 1984, retired in May and is now working under contract while his successor is chosen. The Deputy Director for Operations and Administration was appointed in December 1985, and may be reassigned as early as January 1988. Mr. Dertadian is a Senior Foreign Service Officer whose current position is of no prescribed length. However, as a member of the Foreign Service he would generally not be expected to remain at the head of FBO for the several years it will take to complete the proposed security construction program.

During the subcommittee's hearing, Assistant Secretary Bouchard acknowledged the importance of assuring continuity in FBO's top management and described the Department's current effort to achieve this goal. Mr. Bouchard testified that a new position of deputy to the Deputy Director for Capital Programs is being established. This new position will be filled by a Civil Service employee. According to the Department, the new staff person will be hired, "Hopefully . . . before the end of the calendar year." [62]

The committee views the Department's effort as a constructive step, but believes that more must be done to provide greater continuity in FBO's management. Among the possible alternatives are: (1) reclassifying the top three positions at FBO as Civil Service as vacancies occur, or (2) mandating extended tours of duty for Foreign Service officers in those positions.

F. THE NEED FOR VIGOROUS OVERSIGHT OF FBO'S OPERATIONS

Vigorous and effective oversight is necessary to achieve the dramatic improvements needed in FBO's construction operations. The State Department's top management, the Department's new Office of Inspector General, and Congress must all play a role in this process.

As noted earlier, the State Department has acknowledged that the proposed $2.9 billion security construction program is a massive undertaking by the Department's standards. An expensive initiative under any circumstances, the proposal is especially costly in light of the fiscal constraints imposed by the "Balanced Budget and Emergency Deficit Control Act of 1985." The committee notes, however, that even if funding for the proposed program falls short of the Department's request, the $1.2 billion in FBO construction projects currently in progress still represents a significant investment of the taxpayers' money. It is, therefore, absolutely essential that the top management of the State Department—including the Secretary of State—make a strong personal commitment to improving FBO's performance. The appalling waste and mismanagement that have plagued many FBO construction projects simply must stop.

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[62] Hearing.

Commenting on FBO's plans to correct many of its systemic deficiencies by contracting with private sector firms for construction management expertise, Deputy Program Inspector General Hollingsworth stated:

> . . . Whether or not these actions will allow FBO to manage its largely expanded construction program in an effective and economical manner remains to be seen. This depends both on the competence and integrity of private sector construction and construction management firms, and on FBO's capability to manage and oversee its contracts with these firms. In my judgment, *a critical factor in this process will be the availability of adequate audit resources to independently evaluate the progress of both FBO and the design/construction program on a continuing basis.* (Emphasis added.) [63]

The committee strongly concurs with Mr. Hollingsworth's views on the importance of auditing. It is, therefore, deeply concerned about the relatively small amount of resources devoted to auditing FBO's operations.

Over the past 5 years, the authorized staffing level of the Office of Program Inspector General has ranged from 67 to 98. The responsibilities of the Office, however, have included inspections, audits, and investigations of the State Department's operations in this country as well as at 248 locations overseas. As a result, the Program Inspector General has only been able to devote the equivalent of about one staff person per year over the past several years to auditing FBO. In the subcommittee's hearing, Mr. Hollingsworth called this audit coverage "barely adequate." He identified several areas of FBO's operations needing additional audit work: (1) real estate acquisition, management, and disposal; (2) building maintenance and repair; (3) short and long-term leasing; (4) renovation and capital improvement; and (5) procurement and contracting. Mr Hollingsworth also noted that implementation of the proposed construction program would greatly increase the need for audits of FBO.[64]

Responsibility for auditing FBO's operations and certain other State Department activities will soon be transferred from the Department's Office of Program Inspector General to the new Office of Inspector General, established by Public Law 99-93. (In addition to establishing a new Office of Inspector General subject to the provisions of the Inspector General Act of 1978, P.L. 99-93 changed the name of the then Office of Inspector General to the Office of Program Inspector General. P.L. 99-93 also restricts the Program Inspector General to performing what are generally referred to as "conduct of relations" inspections. These are reviews intended to determine whether the activities and operations of U.S. diplomatic posts overseas are consistent with the foreign policy of the United States. Secretary of State Shultz has authorized the Program Inspector General to continue performing audits and investigations as well as conduct of relations inspections until the new Office of

[63] Hearing.
[64] Hearing.

Inspector General is in operation. The Secretary has made this authorization based on what he describes as his "own inherent authorities to manage the operations of the Department . . ." [65]

Mr. Hollingsworth, who headed a team responsible for planning the new office, told the subcommittee that the Inspector General will need a staff of 180 in order to provide adequate audit coverage. Nineteen of these people would be involved in reviewing diplomatic security matters and FBO operations.

At least initially, however, the Inspector General will have a staff of no more than 44, including 38 positions to be transferred from the Office of Program Inspector General. This level of staffing will inevitably result in less-than-adequate audit coverage of FBO. The committee views the Department's decision on staffing levels for the new Office of Inspector General as extremely shortsighted.

The committee is also very concerned about lengthy delays in implementation of the new Office of Inspector General. While the authorizing legislation was signed into law on August 16, 1985, an Inspector General has still not been appointed.

The committee recommends that the Secretary of State take appropriate action to assure that the Office of Inspector General begins operating as soon as possible. It also recommends that the Secretary significantly increase the level of resources to be provided to the Inspector General.

(NOTE.—The Senate version of the diplomatic security package includes provisions that would abolish the Office of Program Inspector General. As noted earlier, at the time of the committee's consideration of this report, efforts were underway to resolve the differences between the House and Senate versions of the legislation.)

Finally, the committee will continue its active oversight of FBO's operations. Chairman Brooks has requested that GAO assess the adequacy of the State Department's efforts to correct FBO's longstanding construction management deficiencies. The committee also intends to initiate direct monitoring of FBO's construction program. The committee recommends, therefore, that the State Department provide quarterly detailed written reports on FBO's construction operations, including the status of all projects in progress.

V. CONCLUSION

Operating a worldwide construction program in conditions ranging from those found in advanced industrialized nations to those in remote third-world countries is a difficult task. Nevertheless, the committee's review has documented serious and longstanding systemic deficiencies in FBO's operations. Failure to correct these problems would jeopardize efforts to provide the increased security needed for U.S. personnel serving their country overseas. It would also waste valuable tax dollars.

The committee is encouraged by the State Department's current and proposed efforts to improve FBO's performance. Additional corrective actions are needed, however, to achieve an efficient, effective, and economical overseas construction program. Furthermore,

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[65] Hearing.

efforts to improve FBO will succeed only if backed by a strong and sustained personal commitment from the Department's top management. The committee will closely monitor FBO's operations on a continuing basis to assure full accountability in the use of the taxpayer's money.

VI. Findings

1. Serious and longstanding systemic deficiencies in FBO's operations have resulted in many construction projects being plagued by substandard design, poor contracting procedures, shoddy workmanship, inadequate management, lengthy delays, and major cost overruns.
2. Successful implementation of the State Department's proposed security construction program will require a tremendous improvement in FBO's performance. While current and proposed corrective actions appear promising, these efforts must be backed by a strong and sustained commitment from the top management of the Department.
3. Continued frequent turnover in the top management of FBO would seriously threaten the State Department's efforts to improve FBO's operations. While the Department's current plans for assuring greater continuity are a step in the right direction, stronger actions are needed.
4. A significant increase in the Department's audit resources is needed to assure adequate audit coverage of FBO's operations, particularly the proposed security construction program.
5. The State Department has failed to make a persuasive case that the sale of the unfinished ambassador's residence in the Giza section of Cairo was in the U.S. Government's best interests.
6. The U.S. Army Corps of Engineers represents a valuable source of management expertise for the State Department's proposed security construction program.

VII. Recommendations

The committee recommends that the State Department:

1. Implement promptly and completely all of the recommendations in the Program Inspector General's August 1985 report on FBO's construction program. The committee requests that the Department provide, within 30 days, a written report on the status of its efforts to implement these recommendations;
2. Provide the committee with quarterly detailed written reports on FBO's construction operations, including the status of all projects in progress;
3. Establish strong internal controls to monitor the performance of the private sector program managers involved in FBO's construction operations;
4. Take additional actions to assure greater continuity in the top management of FBO;
5. Take appropriate action to get the new Office of Inspector General operating as soon as possible;
6. Significantly increase the level of resources to be provided to the new Office of Inspector General;

7. Utilize the Army Corps of Engineers to the fullest extent practicable in implementing its proposed security construcion program; and

8. Provide the committee with detailed documentation to support its claim that it was required by Egyptian law to complete the sale of the Giza property.

APPENDIX

List of Recomendations Included in Audit of New Construction by Office of Foreign Buildings Operations, August 1985

LIST OF RECOMMENDATIONS

A. Recommendations that can be implemented in the immediate future and witout an increase in resources

1. A/FBO should ensure that project managers are provided copies of all codes, standards, and other publications referenced in construction contracts, prior to the start of consutruction.

2. A/FBO should revise the changes clause in its construction contracts. This revision should clearly specify that no claim for any change shall be allowed for costs incurred more than 20 days before the contract or gives written notice to the U..S Government that instructions received have been considered to be a change to the original contract.

3. A/FBO should establish an internal regulation requiring that for all major construction projects (projects costing in excess of $250,000) performance bonds, or other types of performance guarantees from a surety, at face value of at least 15 percent of the contract, be provided by the contractor. In addition, this regulation should prohibit the lowering of the bond during construction, and, if change orders are issued that significantly raise the contract price, the value of the performance bond should be increased correspondingly.

4. A/FBO construction contracts should not allow for advance payments unless it can be determined that this is the only way that qualified contractors will be interested in the project. In cases where advance payments are made, the contract file should include a statement justifying the reasons for the payment. If, in certain instances, it is in the U.S. Government's interest to assist a contractor in financing the contractors early operations, then such payments could be made but only when they can be directly tied to this contractor's mobilization expense.

5. A/FBO should establish an accident prevention progam for construction projects overseas. A clause should be inserted in construction contracts requiring the contractor to provide an effective accident prevention program.

B. Recommendations that will require additional resources and/or substantial time for full implementation

6. A/FBO should include a clause in all construction contracts requiring the contractor to provide and maintain an effective quality control system. The clause should describe the various types of

inspection of workmanship and testing of materials that must be done, and emphasize that quality control, including work performed by subcontractors, is the responsibility of the contractor.

7. A/FBO should establish a staff adequate in size to inspect all ongoing construction projects on a systematic basis, particularly during critical stages of construction. This staff of individuals knowledgeable in architectural, structural, mechanical, and electrical phases of construction, as well as in construction techniques, would inspect projects to ensure that they are being accomplished in a manner that will ensure a quality building.

8. A/FBO should supplement its staff with additional structural, mechanical, and electrical engineers to assist in performing design analysis for constructibility, and to oversee construction projects. This staff, rather than being assigned to a particular project, could be available to assist in overseeing construction as needed for various projects throughout the world.

9. For large construction projects (e.g. over $5 million), A/FBO should assign full-time inspectors qualified in each of the engineering disciplines to the on-site management staff. Wherever practical, one individual should be dedicated to the contract administration function.

10. A/FBO should develop and issue procedural manuals which would include internal regulations covering the awarding and administering of design and construction contracts, and managing construction projects. These manuals should clearly identify specific procedures that must be followed by individuals involved in the various aspects of construction and should clearly differentiate between guidelines and mandatory requirements.

11. A/FBO should initiate a program for value engineering. Completed designs, wherever time restraints do not preclude this, should be studied by in-house architects or contracted to specialists to determine where changes can be made that will not affect quality but will reduce construction costs.

12. A/FBO should include a value engineering clause in construction contracts that allows the contractor to share in savings achieved through value engineering.

13. A/FBO should issue a policy statement together with A/FBO regulations which includes detailed procedures for negotiating, pricing, and issuing change orders. These regulations should include the following requirements: (a) an independent U.S. Government estimate should be made for each change expected to exceed $25,000, prior to reviewing the contractor's proposal for the changed work; (b) formal memorandums of negotiations should be prepared and maintained on file detailing how the agreed-to price was arrived at; and (c) contract audits should be requested for all change orders expected to exceed $500,000, except where there is sufficient information to determine that an audit is unnecessary and the files document the basis of this determination.

14. A/FBO should not include specified percentages for overhead and profit applicable to changes in construction contracts. Rather, these factors should be negotiated in the same manner as other elements of cost applicable to the change.

15. A/FBO should revise its methods for processing contractors' claims. A policy statement and applicable A/FBO regulations

should be issued prescribing a detailed procedure for handling claims. This procedure should include at a minimum: (a) the types of records that must be kept at the construction site (e.g., daily logs); (b) a system to provide for timely investigation and decision making by those individuals representing the U.S. Government; (c) a procedure for requesting audit services where the claim exceeds $500,000; and (d) preparation of formal memorandums of negotiations detailing the resolution of the claims, i.e., settlement, denial, or withdrawal by the contractor.

16. A/FBO should issue an internal regulation detailing the procedures to be used for all negotiated contracts. These procedures should include the following requirements: (a) descriptions of the training needs and composition of the members of negotiating teams; (b) detailed U.S. Government estimates for contracts expected to exceed $25,000; (c) audits of proposals in excess of $500,000 to be requested or the files documented that an audit was determined to be unnecessary; (d) formal memorandums of negotiations detailing how prices were established; and (e) solicitation for proposals from several sources or documentation in the contract file as to why this was not done.

17. A/FBO should advertise for each specific A&E project or service and require responding firms to submit the detailed information necessary to evaluate their qualifications for the specific project. A/FBO should include A/FBO/CM, A/FBO/AD, and A/FBO/BD personnel in a panel to evaluate and select firms for miscellaneous A&E requirements. This panel should evaluate and make a selection based on the technical qualifications of the firm as provided in response to an advertisment for the specific project or service.

18. A/FBO should establish procedures to evaluate design errors or omissions, and seek remuneration from A&E firms when such errors or omissions result in significant construction contract change orders. These procedures should require that all construction contract change orders be analyzed for design deficiencies. A/FBO should also annotate its files with information regarding design deficiencies for use in future evaluations of A&E firms for A/FBO contracts.

19. A/FBO should establish a dollar limitation for amendments to miscellaneous A&E contracts and a one-year time limit. A/FBO should also require that when these contracts exist for more than one year, or reach the established dollar limit, the Department selection committee be notified of the reasons. A procedure should also be established requiring a well defined specification and scope of work for every project prior to advertisment.

20. A/FBO should issue a policy statement and an internal regulation providing guidance and specific procedures for entrepreneurial projects. Policy and procedures would include at a minimum: (a) the extent of financial analysis that must be performed prior to initiating action to solicit developers; (b) the type and quality of property appraisals that must be obtained; (c) the levels of authority and responsibility for approving projects; (d) the specific qualifications needed by the U.S. Government negotiating team; and (e) a description of the elements of control that must be included in agreements, such as Letters of Credit, performance or payment bonds, etc.